

All language is new and therefore not underlined

REGULATION SECTION 25113

Section 25113 is adopted to read:

§ 25113. Water's-Edge Election.

(a) This regulation shall be applicable to taxable years beginning on or after January 1, 2008.

(b) Definitions. For purposes of Revenue and Taxation Code section 25113 and this regulation, the following definitions are applicable:

(1) Water's-edge group. The water's-edge group means all banks, corporations or other entities whose income and apportionment factors are considered pursuant to Revenue and Taxation Code section 25110 in computing the income of the individual taxpayer for the current taxable year which is derived from or attributable to sources within this state.

(2) Original return. The original return is the last return filed on or before the due date (taking extensions into account) regardless of the form on which it is filed or however it may be denominated. A return filed after the due date (taking extensions into account) regardless of the form on which it is filed or however it may be denominated may be an original return, if no other return has been filed, but it would not be a timely filed, original return.

(3) Timely filed. A timely filed return is one filed on or before the due date (taking extensions into account).

(4) Commencement date. The commencement date of a water's-edge election is the first day of the period for which the election is made. Subsection (c)(6) of this regulation provides rules for taxpayers that have a valid election for taxable years beginning before January 1, 2003.

(5) Net book value. Net book value is equal to an asset's original cost minus depreciation and amortization. Book value means the amount, which an asset is carried on a balance sheet. Depreciation means the systematic write off of the cost of a tangible asset over the asset's useful life. Amortization means the systematic write off of the cost of an intangible asset over the asset's useful life. Book value, depreciation, and amortization will be reflected using United States Generally Accepted Accounting Principles (US GAAP.) If any member of a component unitary group does not maintain its books on US GAAP, the Franchise Tax Board may allow an alternative method of valuation of that member's business assets.

(6) Parent Corporation. A parent corporation of the taxpayer is a corporation that owns or constructively owns stock possessing more than 50 percent of the voting

power of the taxpayer as determined under Revenue and Taxation Code section 25105, subdivisions (e) and (f).

(7) Unitary affiliate group. Unitary affiliate group is all of those corporations that would constitute a unitary group if a water's-edge election were not made.

(8) New unitary affiliate group. New unitary affiliate group is a unitary affiliate group that is created by a new affiliation of two or more corporations, or by the addition of one or more new members to an existing unitary affiliate group.

(9) Component unitary group. Component unitary group is that portion of a group of corporations that have become members of a new unitary affiliate group that were members of their own respective unitary affiliate group prior to entering the new unitary affiliate group, disregarding any corporations that did not become part of the new unitary group.

(10) Business assets. Business assets are assets, including intangible assets, other than stock of a member of the unitary affiliate group, which are used in the conduct of the business of the unitary affiliate group or would produce business income to the unitary affiliate group, if an election were not in place, if the assets were sold.

Business assets are valued at net book value as of the date that electing taxpayers and nonelecting taxpayers or non-taxpayers become members of a new unitary affiliate group. A copy of the taxpayer's valuation of the business assets shall be attached to the return for which the valuation is required by Revenue and Taxation Code section 25113. The Franchise Tax Board may, in its sole discretion, allow an alternative valuation date if it determines that an alternative date would be more appropriate.

(11) Taxpayer. Taxpayer means the individual corporation with a requirement to file under this part. It does not mean the water's-edge group or all the members of the water's-edge group that are required to file under this part.

(12) Good cause. Good cause shall have the same meaning as specified in Treasury Regulation section 1.1502-75(c).

(13) Common parent election. A common parent election may be made by a parent corporation that is an electing taxpayer or by an officer or other authorized agent of either a parent corporation of a nonelecting taxpayer or another corporation with authority to bind a nonelecting taxpayer to an election. Either subsection (c)(2)(A)1. or 2. of this regulation would constitute a common parent election.

(c) Electing water's-edge.

- (1) To make the water's-edge election permitted by Revenue and Taxation Code section 25110, a taxpayer must make an election on a timely filed, original return for

the year of the election. The election must be made by every member of the self-assessed combined reporting group that is subject to taxation under this part. The initial election must be for an 84-month period. A water's-edge election shall remain in effect until terminated.

- (2) An election made on a group return of a self-assessed combined reporting group is an election by each taxpayer member included in that group return. No election will have been made if a taxpayer member of the combined reporting group files a separate return in which no election is made and subsection (c)(3) does not apply.

(A) A taxpayer that fails to make an election on its own timely filed, original return shall be deemed to have elected if any of the following apply:

1. It has a parent corporation that is an electing taxpayer that included the income and apportionment factors of the nonelecting taxpayer in the self-assessed combined reporting group reflected in the electing parent's timely filed, original return, including a group return.

2. The income and apportionment factors of the nonelecting taxpayer are reflected in the self-assessed combined reporting group of a timely filed, original return of an electing taxpayer, and the notification of election filed by the electing taxpayer pursuant to Revenue and Taxation Code section 25113, subdivision (a)(2) is signed by an officer or other authorized agent of either a parent corporation of the nonelecting taxpayer or another corporation with authority to bind the nonelecting taxpayer to an election.

EXAMPLE: 1. Corporation P, a California taxpayer and a calendar year taxpayer, has a subsidiary, Corporation A, who is also a California taxpayer and calendar year taxpayer.

- A. Corporation P makes a common parent water's-edge election and includes its subsidiary Corporation A in the combined report used to determine its California income. Corporation A files a separate return using a worldwide combined report that includes Corporation P. Corporation A is deemed to have elected.
- B. Corporation P, a California taxpayer, timely files a single group return on a combined basis for all members of the water's-edge group and includes the income and apportionment factors (both numerators and denominators) of Corporation A. Corporation A files a separate return and files on a worldwide basis. Corporation A is deemed to have elected.

EXAMPLE: 2. Corporation P has subsidiaries, Corporations A, B and C. Corporations A and C are California taxpayers, Corporations P and B are not.

- A. Corporation B's President has a power of attorney for every member of Corporation P's commonly controlled group, including Corporation A.

Corporation C timely files its own return on a combined basis including the income and factors of Corporation A and other members of the water's-edge group. Corporation B's President signs a common parent election that lists all taxpayer members of Corporation P's commonly controlled group as making a water's-edge election. Corporation A files a separate return on a worldwide basis. Corporation A is deemed to have elected.

- B. Corporation P's Chief Executive Officer signs the notification of election and indicates that it is making a common parent election which Corporation B, a taxpayer member of the water's-edge group, includes with its timely filed, original return filed on a water's-edge basis. Corporation A files a separate return on a worldwide basis. Corporation A is deemed to have elected.

EXAMPLE: 3. Corporation P is not a California taxpayer, but it has subsidiaries A, B and C that are taxpayers and are part of its unitary business. No common parent election has been filed prior to the due date (taking extensions into account) for filing a return. After the due date (taking extensions into account), a delinquent original California return is filed with a common parent election by Corporation P, stating that it now believes it had nexus in California. Because the election was not made on a timely filed, original return, there is no valid election.

EXAMPLE 4. Corporation P, the parent corporation and a calendar year taxpayer, makes a common parent water's-edge election and includes its subsidiary, Corporation A, also a calendar year taxpayer, as a member of the water's-edge group. Corporation P and Corporation A have different fiscal years. Corporation P's taxable year ends March 31 and Corporation A's taxable year ends December 31. Corporation P files its March 31, 2008 taxable year return on January 15, 2009 on a combined basis, which includes Corporation A. Corporation A files its December 31, 2008 return on October 15, 2009 on a separate company worldwide basis. Corporation A is deemed to have elected. Corporation A's and Corporation P's election commencement date is determined in accordance with the provisions of subsection (g) of this regulation.

3. If a corporation that is a member of a combined reporting group is not itself subject to taxation under Part 11 in the year for which the water's-edge election is made, but subsequently becomes subject to taxation under Part 11, that corporation shall be deemed to have elected with the other taxpayer members of the combined reporting group.

4. A corporation that is a nonelecting taxpayer and is subsequently proved to be member of the water's-edge group pursuant to a Franchise Tax Board audit determination shall be deemed to have elected if the value of the total business assets of the electing taxpayers is greater than those of the non-electing taxpayers.

For purposes of applying the business asset test of this subsection, the term "business assets" shall have the same meaning as Revenue and Taxation Code section 25113, subdivision (c)(6)(A), except that the business assets of other

members of the unitary affiliate group that are not taxpayers shall not be taken into account.

(B) A taxpayer that is engaged in more than one apportioning trade or business as defined in Revenue and Taxation Code section 25128, subdivision (d)(6), may make a separate election for each apportioning trade or business.

(3) Validity of Election. The election shall be considered valid if the following are satisfied:

(A) The tax is computed in a manner that is consistent with a water's-edge election, and

(B) The taxpayer files its return on a form 100W (S Corporations file a form 100S) and attaches a form 100-WE.

(C) In place of subsection (c)(3)(B), the Franchise Tax Board may consider other objective evidence of the making of a water's-edge election, such as:

1. A statement attached to the timely filed, original return indicating a water's-edge election is being made, or
2. The taxpayer's timely filed, original return includes one or more substantially completed forms associated with a water's-edge combined report, such as FTB form 1115, 2416, 2424, or their successors.

(4) Time of making the election.

(A) The election must be made on a timely filed, original return.

(B) Timely filings which only supplement a previously filed return, or correct mathematical or other errors, shall be considered as incorporating the previously filed return, to the extent not inconsistent, and shall be treated as the original return for purposes of making a water's-edge election if they contain objective evidence that supports the conclusion that a water's-edge election was intended as provided in subsection (c) of this regulation. Any filing described in this subsection (c) of this regulation that clearly reflects an intent to withdraw an election made on previously filed return shall be treated as an original return.

EXAMPLE 1: Corporation A is a calendar year taxpayer. Its return is due March 15. But if it files its return on or before October 15, an extension is automatically granted to October 15. If it fails to file a return by October 15, no extension exists. Under the paperless extension process, the return is timely if it is filed on or before October 15.

- a. Corporation A files its original return on October 15 of the year. The original return is timely filed, and any water's-edge election contained therein shall be effective for the year for which the return is filed.

b. Corporation A files its original return on May 15 of the year. The original return is timely filed, and any water's-edge election contained therein shall be effective for the year for which the return is filed.

c. Corporation A files a return on May 15 and files a second return on October 15. Corporation A's original return was filed on October 15. The water's-edge election must be made by that time. If Corporation A's May 15th filing makes a water's-edge election, and the election is withdrawn in the October 15th filing, the election made on May 15th has no effect. If Corporation A's May 15th filing did not make a water's-edge election, but a water's-edge election is made on the October 15th filing, Corporation A has made a water's-edge election.

EXAMPLE 2: Corporation B, a calendar year taxpayer, files a return on February 15. Corporation B's return is treated as being filed on March 15, and March 15 is the date the election is considered to have been made. Any return filed after March 15 (the due date of the return) will be considered an amended return.

EXAMPLE 3: Corporation C, a calendar year taxpayer, has a due date for its return of March 15. It files a return on February 15 and files a second return on March 10. The return filed on March 10 is treated as the original return for the year. The election to file on a water's-edge basis must be made on the March 10 filing to be effective. If Corporation C's February 15 filing makes a water's-edge election and the March 10 filing does not make an election, the election made on the February 15 return has no effect. If Corporation C's February 15th filing did not make a water's-edge election, and a water's-edge election is made on the March 10th filing, Corporation C has made a water's-edge election.

(5) A copy of the original election should be attached to all subsequent returns filed during the election period.

(6) Corporations that have a valid election for taxable years beginning before January 1, 2003, and are required to file on a water's-edge basis for taxable years beginning on or after January 1, 2003 due to that election, will continue to file on a water's-edge basis and will be deemed to have elected under Revenue and Taxation Code section 25113 for taxable years beginning on or after January 1, 2003. The commencement date, as elected under Revenue and Taxation Code section 25111, remains in effect.

EXAMPLE 1: Corporation A, a calendar year taxpayer, elected to file on a water's-edge basis starting January 1, 2000. For taxable years beginning on or after January 1, 2003, Corporation A must continue to file on a water's-edge basis and is deemed to have elected under the new statute. Under Revenue and Taxation

Code section 25111, subdivision (a), a taxpayer would always have an 84-month contract on its anniversary date unless it filed a notice of nonrenewal. Although Corporation A originally entered into a water's-edge contract commencing on January 1, 2000, an additional year would have been added to the contract each year unless a notice of nonrenewal was filed pursuant to Revenue and Taxation Code section 25111. The election commencement date for purposes of Revenue and Taxation Code section 25113 is January 1, 2002.

For the year beginning January 1, 2009, and each year thereafter, Corporation A may file on a water's-edge basis without being subject to a new 84-month election period or may terminate its election by filing on a worldwide basis.

EXAMPLE 2: Corporation B, a calendar year taxpayer, made a water's-edge election beginning January 1, 1994, and filed a notice of nonrenewal to end the contract on December 31, 2001. Corporation B did not file a new contract for the taxable year ended on December 31, 2002, but continued to file on a water's-edge basis on a timely filed, original return that contained other objective evidence of an intended water's-edge election. Corporation B has a new water's-edge election with a commencement date of January 1, 2002. Corporation B may not terminate its water's-edge election for any year prior to the expiration of the 84-month period without the Franchise Tax Board's consent as provided under Revenue and Taxation Code section 25113, subdivision (c)(9). It could terminate without the Franchise Tax Board's consent only after the 84-month period that ends December 31, 2008.

Corporation B's election, entered into for the 1994 taxable year, ended on December 31, 2001, because the filing of the notice of nonrenewal prevented automatic annual renewal of the contract. However, for the taxable year ended December 31, 2002, Corporation B had a valid new water's-edge contract, because there was substantial performance of the requirements for entering into a water's-edge contract. Therefore, Corporation B had a new water's-edge contract with a commencement date of January 1, 2002. As a consequence, under Revenue and Taxation Code section 25111, subdivision (f), and section 25113, subdivision (f), Corporation B's commencement date of the election is January 1, 2002. Because Corporation B's election will not have been in existence for 84 months until after December 31, 2008, it must obtain the Franchise Tax Board's consent to terminate the election before then.

EXAMPLE 3: Corporation C elected to file on a water's-edge basis beginning April 1, 1995, for its fiscal year ended March 31, 1996. Corporation C filed a notice of nonrenewal to end the contract on March 31, 2003. For the taxable year ended March 31, 2004, Corporation C filed on a worldwide basis. Corporation C may make a water's-edge election without the Franchise Tax Board's consent for a taxable year that begins within the 84-month period after March 31, 2003.

Corporation C's election contract under Revenue and Taxation Code section 25111 ended on March 31, 2003, due to the previously filed notice of nonrenewal.

Revenue and Taxation Code section 25113 is operative with respect to Corporation C for its taxable years beginning on or after April 1, 2003. Therefore, Corporation C could have made an election under Revenue and Taxation Code section 25113, but it chose to file its return for the taxable year ended March 31, 2004, on a worldwide basis.

The filing on a worldwide basis for the year ended March 31, 2004, did not constitute a "termination" of a water's-edge election under Revenue and Taxation Code section 25113, because Corporation C had not made a water's-edge election for any taxable year beginning on or after January 1, 2003. For taxable years beginning after March 31, 2003, Corporation C may file on a worldwide basis and may make a water's-edge election under Revenue and Taxation Code section 25113 without requesting the Franchise Tax Board's consent to "re-elect."

EXAMPLE 4: Corporation D elected to file on a water's-edge basis beginning April 1, 1996, for its fiscal year ended March 31, 1997. Corporation D filed a notice of nonrenewal to end the contract on March 31, 2004. For the taxable year ended March 31, 2005, Corporation D filed on a worldwide basis. Corporation D effectively terminated its water's-edge election pursuant to Revenue and Taxation Code section 25113, subdivision (c)(9), when it filed on a worldwide basis for the taxable year ended March 31, 2005. Corporation D's filing of the notice of nonrenewal under section 25111 has no effect because it caused the water's-edge contract to end on a date that falls within a taxable year that begins on or after January 1, 2003. Corporation D would not be able to make another election without the Franchise Tax Board's consent until 84 months have passed from March 31, 2004.

EXAMPLE 5: Corporation E elected to file on a water's-edge basis beginning January 1, 1994, and filed a notice of nonrenewal to end the contract on December 31, 2006. Corporation E must request the Franchise Tax Board's consent to terminate the election prior to December 31, 2006.

Under Revenue and Taxation Code section 25111, subdivisions (d) and (e), Corporation E's existing election remains in effect for the "balance of the period remaining since the original election or the last renewal of the election" unless it serves written notice of nonrenewal at least 90 days prior to the annual renewal date. Under Revenue and Taxation Code section 25111, subdivision (a), a taxpayer would always have an 84-month contract on its anniversary date, unless it filed a notice of nonrenewal. Although Corporation E originally entered into a water's-edge contract commencing on January 1, 1994, an additional year would have been added to the contract each year until a notice of nonrenewal was filed. In order to terminate its contract for years after December 31, 2006, Corporation E would have had to complete a contract period of 84 months on December 31, 2006. As of January 1, 2003, Corporation E is deemed to have elected under Revenue and Taxation Code section 25113, with a commencement date of January 1, 2000, 84 months prior to December 31, 2006.

Under Revenue and Taxation Code section 25113, subdivision (f), the commencement date of the election made in a prior year under Revenue and Taxation Code section 25111 is treated as the commencement date for purposes of applying Revenue and Taxation Code section 25113. Because Corporation E's election would not have been in effect for longer than 84 months, it may not terminate the election as permitted under Revenue and Taxation Code section 25113, subdivision (c)(9), by timely filing an original tax return on form FTB 100 on a worldwide basis until after December 31, 2006. In order to terminate the election prior to December 31, 2006, the taxpayer must request and receive consent from the Franchise Tax Board under Revenue and Taxation Code section 25113, subdivision (c)(10).

(d) Termination.

(1) A water's-edge election may be terminated after the expiration of the initial 84-month period. This termination does not require Franchise Tax Board consent.

a. The termination shall be made on a timely filed, original return computed on a worldwide basis for the first year in which the water's-edge election is to be terminated.

b. The termination shall be made by every taxpayer that is a member of the water's-edge group.

c. The termination shall be effective if the termination is made in the same manner as the election provided under Revenue and Taxation Code section 25113, subdivisions (a) and (b).

d. Written notification of termination shall be made on a form prescribed by the Franchise Tax Board. The Franchise Tax Board may accept other objective evidence of termination of the water's-edge election such as:

1. A timely filed, original return computed on a worldwide basis using form FTB 100 rather than form FTB 100W, or

2. A statement attached to the timely filed, original return indicating a water's-edge election is being terminated.

(2) The Franchise Tax Board may consent to terminate a water's-edge election prior to the expiration of the 84-month period if a request is made demonstrating good cause.

a. A request to terminate a water's-edge election shall be made on a form prescribed by the Franchise Tax Board and be filed no later than the 120th day prior to the due date of the return for which the termination would be effective, including extensions. The request shall be filed

separate from any tax return and shall be mailed to the address listed in the form instructions for the notification of termination form prescribed by the Franchise Tax Board. The request shall include information and documentation of the basis for requesting termination.

b. If the Franchise Tax Board takes no action or requests no additional information within 90 days of the filing of the request to terminate the water's-edge election, the request shall be deemed to be disallowed.

c. If the request is granted, the Franchise Tax Board will send a notification of the termination. The termination will be effective for the taxable year in which good cause occurred. Thereafter, the taxpayer will be required to file on a worldwide basis for at least 84 months before making another water's-edge election.

d. A request to terminate a water's-edge election in order to permit the state to contract with an expatriate corporation, or its subsidiary, pursuant to paragraph (2) of subdivision (b) of Section 10286 of the Public Contract Code, shall be made on a form prescribed by the Franchise Tax Board. The request shall be filed separate from any tax return and shall be mailed to the address listed in the form instructions for the form for requesting permission to terminate prescribed by the Franchise Tax Board.

1. A request to terminate a water's-edge election under Revenue and Taxation Code section 25113, subsection (c)(10)(B), shall be made on a form prescribed by the Franchise Tax Board and be filed no later than the 120th day prior to the due date of the return for which the termination would be effective, including extensions. All members of the water's-edge group must make the request. Such request shall also include source documentation to support the request.

2. A water's-edge election terminated pursuant to this subsection shall be effective for the year in which the expatriate corporation, or its subsidiary, enters into the contract with the state.

3. The Franchise Tax Board shall consent to a properly filed and documented request to terminate pursuant to Revenue and Taxation Code section 25113, subsection (c)(10)(B).

e. The taxpayer may withdraw its request at any time prior to the Franchise Tax Board granting permission.

(3) The water's-edge election shall be automatically terminated in certain instances. Written notification of termination shall be made by every taxpayer that is a member of the water's-edge group on a form prescribed by the

Franchise Tax Board.

- a. If an electing taxpayer and a nonelecting taxpayer become members of a new unitary affiliate group and the value of the total business assets of the nonelecting taxpayer (and affiliates, if any) is greater than those of the electing taxpayer (and affiliates, if any), the election shall be automatically terminated.
- b. If an electing taxpayer and a nonelecting taxpayer become members of a new unitary affiliate group during the taxable year, the electing taxpayer (and affiliates, if any) shall compute its tax liability on a water's-edge basis until the termination. The electing taxpayer (and affiliates, if any) shall compute its tax liability for the remaining portion of the taxable year after the termination as part of the nonelecting taxpayer's unitary affiliate group. The nonelecting taxpayer (and affiliates, if any) shall compute its tax liability on a worldwide basis for the entire year.

(e) Re-election.

(1) A water's-edge election remains in effect until terminated. If a taxpayer terminates its water's-edge election and returns to filing on a worldwide basis, then another water's-edge election may not be made for any taxable year that begins within the 84-month period following the last day of the election period that was terminated. However, the Franchise Tax Board may waive the application of this rule for good cause.

(2) A request to re-elect water's-edge shall be made on a form prescribed by the Franchise Tax Board and be filed no later than the 90th day prior to the due date of the return for which the re-election would be effective, including extensions. The request shall be filed separate from any tax return and shall be mailed to the address listed in the form instructions for the form for requesting re-election prescribed by the Franchise Tax Board. The request shall include information and documentation of the basis for requesting re-election.

- a. If the Franchise Tax Board takes no action or requests no additional information within 60 days of the filing of the request to re-elect water's-edge, the request shall be deemed to be disallowed.
- b. If the Franchise Tax Board approves the request for re-election, the taxpayers must then make a water's-edge election as provided in subsection (c). Such election will be effective for the taxable year in which good cause occurred. Consent given by the Franchise Tax Board will not be retroactive.
- c. The taxpayer may withdraw its request at any time prior to the Franchise Tax Board granting permission.

- (3) Consent for re-election is not required if the election was terminated under Revenue and Taxation Code section 25113, subdivisions (c)(2), (4), and (5). In this case, taxpayers may simply make an election as provided in Revenue and Taxation Code section 25113, subdivisions (a) and (b).
- (4) Consent for re-election is not required if the 84-month period following the last day of an election period that was terminated has passed. Taxpayers may simply make an election as provided in Revenue and Taxation Code section 25113, subdivisions (a) and (b).

(f) Election, those affected.

(1) In general. The water's-edge election, to be effective, must be made by all corporations required to file under this part that are part of the water's-edge group. A taxpayer or a group of affiliated taxpayers that is engaged in more than one unitary business may make a water's-edge election with respect to one or more of the businesses, but it need not elect for all of its businesses.

EXAMPLE: Corporations A and B are members of an affiliated group which includes Corporations C, D, E and F, all incorporated in the United States, and Corporations G, H and I, all incorporated outside of the United States. Corporations A and B are taxpayers, but are not engaged in the same unitary business. Corporations G, H and I have no factors in the United States, no United States source income, and have no Subpart F income. Corporations A, C, D and G are engaged in one unitary business. Corporations B, E, F, H and I are engaged in a separate unitary business. Either Corporation A or B may elect to file on a water's-edge basis pursuant to Revenue and Taxation Code section 25110. It is not necessary for both Corporations A and B to make a water's-edge election.

(2) In general, the water's-edge filing status of a combined reporting group that has changes in affiliation will depend upon the status of the taxpayer (and affiliates, if any) with the greater value of total business assets.

(A) If one or more electing taxpayer members of a combined reporting group for any reason leave the group, the water's-edge election remains in effect as to the departing taxpayer members and any remaining taxpayer members.

(B) If electing taxpayers with different election commencement dates become members of a new group, the election commencement date of the new group shall be the commencement date of the taxpayer (and affiliates, if any) whose total business assets are the largest.

(C) If an electing taxpayer and a non-electing taxpayer or a non-taxpayer become members of a new unitary group, the nonelecting taxpayer shall be

deemed to have elected if the value of the total business assets of the electing taxpayer (and affiliates, if any) is greater than those of the non-electing taxpayer or non-taxpayer (and affiliates, if any.) Otherwise, the election shall automatically be terminated at the time the electing members become part of the combined report.

(D) If two non-electing taxpayers with different termination dates become members of a new group, the termination date, together with any associated restrictions on re-election, of the taxpayer (and affiliates, if any) whose total business assets are the largest shall be the termination date of the new group.

EXAMPLE 1: Corporation A, an electing taxpayer, and its unitary subsidiaries are acquired by Corporation B, a non-taxpayer and its non-taxpayer unitary subsidiaries, that have the larger total value of business assets than those of Corporation A's group and become instantly unitary. The new unitary group will file on a worldwide basis as of the date of combination because Corporation B's group has the larger total value of business assets than Corporation A's group and the water's-edge election is terminated. However, if the new group wants to file on a water's-edge basis, the taxpayer members may re-elect without Franchise Tax Board consent for the year in which the election was terminated or any year thereafter, with a new commencement date for the 84-month election period. If the re-election is for the year in which the group becomes properly combined, the commencement date will be the date of combination.

EXAMPLE 2: Corporation B, a nonelecting taxpayer, and its unitary subsidiaries are acquired by Corporation A, an electing taxpayer and its unitary subsidiaries, that has the larger total value of business assets than those of Corporation B's group. In the year the entire group is properly combined, the group will file on a water's-edge basis because Corporation A's group has the larger total value of business assets than Corporation B's group. The start date of the deemed election is the commencement date of Corporation A's election.

EXAMPLE 3: Corporation A and its unitary subsidiaries' election has been terminated and the group becomes a member of Corporation B's unitary group that includes one or more non-electing taxpayers that have no restrictions upon their ability to elect. The total value of business assets of Corporation A and its unitary subsidiaries is larger than that of Corporation B's group. All members of the new Corporation B group that includes Corporation A will be restricted from making a new election for the period of time for which Corporation A is restricted.

EXAMPLE 4: Same facts as EXAMPLE 3, except that Corporation B's taxpayer members have no restrictions upon their ability to elect and have the larger total value of business assets. In this situation, none of the taxpayer members of the new Corporation B group that includes Corporation A will be subject to any restrictions on making a new water's-edge election.

(g) Effect of different fiscal years. In the case of taxpayers that are on different fiscal years, each member of the water's-edge group shall make the election upon its timely filed, original return for the taxable year for which the election is being made. The election shall become effective as of the beginning of the taxable year of the member of the water's-edge group that files its return and election and has the latest taxable year end. The 84-month election period for each member of the water's-edge group will run from the date that the election becomes effective, i.e., the beginning of the taxable year of the last member of the water's-edge group to elect.

Each taxpayer in the group shall calculate its tax on a worldwide basis for that portion of the year between the beginning of its taxable year and the beginning of the taxable year of the last member of the group to make the election, and on a water's-edge basis for the remainder of the taxable year.

EXAMPLE: Corporations A and B are California taxpayers engaged in a unitary business and wish to make a water's-edge election. Corporation A's taxable year ends December 31 and Corporation B's taxable year ends March 31. Corporation A files an election for its taxable year ended December 31, 2007, on its return filed on October 15, 2008. Corporation B files an election for its taxable year ended March 31, 2008, on its return filed on January 15, 2009.

Corporation A's 84-month election period begins April 1, 2007, the beginning of the taxable year of the last member of the group to elect. Corporation A will file its return for the taxable year ending December 31, 2007, apportioning its income to California on a worldwide basis for the period from January 1, 2007, through March 31, 2007, and on a water's-edge basis for the period from April 1, 2007, through December 31, 2007. Corporation B will file its return for the taxable year ending March 31, 2008, apportioning its income to California on a water's-edge basis for its entire taxable year.

Note: Authority cited: Section 19503, Revenue and Taxation Code.

Reference: Section 25113, Revenue and Taxation Code.